

London Borough of Merton Pension Fund

Year ending 31 March 2015

Audit Plan

March 2015

Ernst & Young LLP



General Purposes Committee
Merton Council
Merton Civic Centre
London Road
Morden
SM4 5DX

9 March 2015

Dear Committee Members

Audit Plan – Merton Pension Fund

We are pleased to attach our Audit Plan which sets out how we intend to carry out our responsibilities as auditor. Its purpose is to provide the General Purposes Committee with a basis to review our proposed audit approach and scope for the 2014/15 audit in accordance with the requirements of the Audit Commission Act 1998, the Code of Audit Practice, Standing Guidance, auditing standards and other professional requirements. It is also to ensure that our audit is aligned with the Committee's service expectations.

This plan summarises our initial assessment of the key risks driving the development of an effective audit for the Pension Fund, and outlines our planned audit strategy in response to those risks.

We welcome the opportunity to discuss this plan with you at your June 2015 Committee and to understand whether there are other matters which you consider may influence our audit.

Yours faithfully

Baldeep Singh
Partner
For and behalf of Ernst & Young LLP
Enc

Contents

1. Overview	1
2. The Local Audit and Accountability Act 2014	3
3. Financial statement risks	4
4. Our audit process and strategy.....	6
5. Independence.....	9
Appendix A Fees.....	11
Appendix B UK required communications with those charged with governance	12

In March 2010 the Audit Commission issued a revised version of the 'Statement of responsibilities of auditors and audited bodies' (Statement of responsibilities). It is available from the Chief Executive of each audited body and via the [Audit Commission's website](#).

The Statement of responsibilities serves as the formal terms of engagement between the Audit Commission's appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The Standing Guidance serves as our terms of appointment as auditors appointed by the Audit Commission. The Standing Guidance sets out additional requirements that auditors must comply with, over and above those set out in the Code of Audit Practice 2010 (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Annual Plan is prepared in the context of the Statement of responsibilities. It is addressed to the Audit Committee, and is prepared for the sole use of the audited body. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure – If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

1. Overview

Context for the audit

This Audit Plan covers the work that we plan to perform to provide you with:

Our audit opinion on whether the financial statements of the London Borough of Merton Pension Fund give a true and fair view of the financial position as at 31 March 2015 and of the income and expenditure for the year then ended;

When planning the audit we take into account several key inputs:

Strategic, operational and financial risks relevant to the financial statements;

Developments in financial reporting and auditing standards;

The quality of systems and processes;

Changes in the business and regulatory environment; and

Management's views on all of the above.

We held planning meetings with the Treasury and Insurance Manager on 3 and 19 February 2015 in which we discussed the results to date and we understand that there are no significant changes in the investments, contributions or membership of the Scheme.

By considering these inputs, our audit is focused on the areas that matter and our feedback is more likely to be relevant to the Pension Fund. Our audit will also include the mandatory procedures that we are required to perform in accordance with applicable laws and auditing standards.

In part three of this plan we provide more detail on the above areas and we outline our plans to address them. Our proposed audit process and strategy are summarised below and set out in more detail in section four.

We will provide an update to the General Purposes Committee on the results of our work in these areas in our report to those charged with governance scheduled for delivery in September 2015.

Our process and strategy

Financial statement audit

We consider materiality in terms of the possible impact of an error or omission on the financial statements and set an overall planning materiality level. We then set a tolerable error to reduce the probability that the aggregate of uncorrected and undetected misstatements exceeds planning materiality to an appropriately low level. We also assess each disclosure and consider qualitative issues affecting materiality as well as quantitative issues.

To the fullest extent permissible by auditing standards, we will seek to rely on the work of internal audit wherever possible.

2. The Local Audit and Accountability Act 2014

The Local Audit and Accountability Act 2014 (the 2014 Act) closes the Audit Commission and repeals the Audit Commission Act 1998.

The 2014 Act requires the Comptroller and Auditor General to prepare a Code of Audit Practice. This must be laid before Parliament and approved before 1 April 2015.

Although this new Code will apply from 1 April 2015, transitional provisions within the 2014 Act provide for the Audit Commission's 2010 Code to continue to apply to audit work in respect of the 2014/15 financial year. This plan is therefore prepared on the basis of the continued application of the 2010 Code of Audit Practice throughout the 2014/15 audit.

3. Financial statement risks

We outline below our assessment of the financial statement risks facing the Pension Fund, identified through our knowledge of the Pension Fund’s operations and discussion with those charged with governance and officers.

At our meeting, we will seek to validate these with you.

Significant risks (including fraud risks)	Our audit approach
Risk of management override	
<p>As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.</p>	<p>Our approach will focus on:</p> <ul style="list-style-type: none"> Testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements Reviewing accounting estimates for evidence of management bias, and Evaluating the business rationale for significant unusual transactions
Other financial statement risks	
Changes to the Local Government Pension Scheme	
<p>The 1st of April 2014 marked the start of a new pension scheme which all members of the LGPS automatically joined. Benefits accrued before 1 April 2014 were protected. Key changes impacting on our financial statements audit are:</p> <ul style="list-style-type: none"> • Benefits payable for service from 1 April 2014 will be calculated on a career average basis. • There are an increased number of salary bands, which are used to determine the level of employee contributions with a maximum employee contribution rate of 12.5% <p>There is a risk that benefits payable or employee contributions may be incorrectly calculated if system parameters were not correctly updated.</p>	<p>Our approach will focus on:</p> <ul style="list-style-type: none"> Using membership data and known parameters to undertake a predictive analytical review for benefits payable and employee contributions and critically comparing our predictions with the year-end figures. Walking through benefit payables and employee contribution cases to update our process understanding Substantively testing a sample of benefits paid to ensure calculations are correct Substantively testing a sample of employee contributions to ensure calculations are correct.

There are no other financial statement risks arising from our planning and work to date.

Respective responsibilities in relation to fraud and error

We would like to take this opportunity to remind you that management has the primary responsibility to prevent and detect fraud. It is important that management, with the oversight of those charged with governance, has a culture of ethical behaviour and a strong control environment that both deters and prevents fraud.

Our responsibility is to plan and perform audits to obtain reasonable assurance about whether the financial statements as a whole are free of material misstatements whether caused by error or fraud. As auditors, we approach each engagement with a questioning mind that accepts the possibility that a material misstatement due to fraud could occur, and design the appropriate procedures to consider such risk.

Based on the requirements of auditing standards our approach will focus on:

Identifying fraud risks during the planning stages;

Enquiry of management about risks of fraud and the controls to address those risks;

Understanding the oversight given by those charged with governance of management's processes over fraud;

Consideration of the effectiveness of management's controls designed to address the risk of fraud;

Determining an appropriate strategy to address any identified risks of fraud; and

Performing mandatory procedures regardless of specifically identified fraud risks.

We will consider the results of the National Fraud Initiative and may refer to it in our reporting to you.

4. Our audit process and strategy

4.1 Objective and scope of our audit

Under the Audit Commission's Code of Audit Practice (the 'Code') our principal objectives are to review and report on, the Pension Fund's financial statements.

Our objective is to form an opinion on the financial statements under International Standards on Auditing (UK and Ireland).

4.2 Audit process overview

Our audit involves:

assessing the key internal controls in place and testing the operation of these controls;

where relevant, review and re-performance of the work of your internal auditors;

reliance on the work of experts in relation to areas such as valuation of the investments of the Pension Fund; and

substantive tests of detail of transactions and amounts.

Processes

Our initial assessment of the key processes across the entity has identified the following key processes, both manual and IT:

Contributions receivable

Fund administration - Lump sum and retirement benefits

Transfers in and out of the Pension Fund

Cash and bank processes

Pension payroll

Investments; and

Financial statements close procedures.

Analytics

We will use our computer-based analytics tools to enable us to capture whole populations of your financial data, and support our work on the completeness of your accounting records and in our work on review of journal entries. These tools:

Help identify specific exceptions and anomalies which can then be subject to more traditional substantive audit tests

Give greater likelihood of identifying errors than random sampling techniques.

We will carry out this work in conjunction with that for the Merton Council audit. We will report the findings from our process and analytics work, including any significant weaknesses or inefficiencies identified and recommendations for improvement, to management and the General Purposes Committee.

Internal audit

As in prior years, we will review internal audit plans and the results of their work. We will reflect the findings from these reports, together with reports from any other work completed in the year, in our detailed audit plan, where we raise issues that could have an impact on the year-end financial statements

Use of experts

We will use specialist EY resource as necessary to help us to form a view on judgments made in the financial statements.

Use of Administering Authority Payroll Data

As the majority of contributions paid to the Pension Fund are from the Council as administering authority, we would request access to salary data for the Council's employees to assist us with the audit.

Mandatory procedures required by auditing standards

As well as the financial statement risks outlined in section three, we must perform other procedures as required by auditing, ethical and independence standards, the Code and other regulations. We outline below the procedures we will undertake during the course of our audit.

Procedures required by standards

Addressing the risk of fraud and error;

Significant disclosures included in the financial statements;

Entity-wide controls;

Reading other information contained in the financial statements and reporting whether it is inconsistent with our understanding and the financial statements; and

Auditor independence.

Procedures required by the Code

Reviewing, and reporting on as appropriate, other information published with the financial statements, including the Annual Report

4.3 Materiality

For the purposes of determining whether the financial statements are free from material error, we define materiality as the magnitude of an omission or misstatement that, individually or in aggregate, could reasonably be expected to influence the users of the financial statements. Our evaluation requires professional judgement and so takes into account qualitative as well as quantitative considerations implied in the definition. We have determined that overall materiality for the financial statements of the Pension Fund is £4,722,430 based on 1% of net assets.

We will communicate uncorrected audit misstatements greater than £236,122 to you.

The amount we consider material at the end of the audit may differ from our initial determination. At this stage, however, it is not feasible to anticipate all the circumstances that might ultimately influence our judgement. At the end of the audit we will form our final opinion by reference to all matters that could be significant to users of the financial statements, including the total effect of any audit misstatements, and our evaluation of materiality at that date.

4.4 Fees

The Audit Commission has published a scale fee for all authorities. This is defined as the fee required by auditors to meet statutory responsibilities under the Audit Commission Act in accordance with the Code of Audit Practice 2010. The indicative fee scale for the audit of the Pension Fund is £21,000.

4.5 Your audit team

The engagement team is led by Baldeep Singh, who is a partner in EY's pensions assurance team. Baldeep is supported by Michael Yeats who is responsible for the day-to-day direction of audit work and is the key point of contact for the Finance team.

Paul King is the director leading our overall engagement with Merton Council and our relationship with the General Purposes Committee.

4.6 Timetable of communication, deliverables and insights

We have set out below a timetable showing the key stages of the audit. The timetable includes the deliverables we have agreed to provide to the Pension Fund through the General Purposes Committee's cycle in 2014/15. These dates are determined to ensure our alignment with the Audit Commission's rolling calendar of deadlines.

From time to time matters may arise that require immediate communication with the General Purposes Committee and we will discuss them with the Committee Chair as appropriate.

Following the conclusion of our audit we will prepare an Annual Audit Letter to communicate the key issues arising from our work to the Pension Fund and external stakeholders, including members of the public.

Audit phase	Timetable	Committee timetable	Deliverables
High level planning	November - December 2014	November 2014	Audit Fee letter (sent 29 April 2014) Progress Report
Risk assessment and setting of scopes	January – February 2015	March 2015	Audit Plan
Testing routine processes and controls	January – February 2015	June 2015	Progress Report
Year-end audit	June – July 2015		
Completion of audit	September 2015	September 2015	Report to those charged with governance via the Audit Results Report Audit report (including our opinion on the financial statements). Audit completion certificate
Conclusion of reporting	November 2015	November 2015	Annual Audit Letter

In addition to the above formal reporting and deliverables we will seek to provide practical business insights and updates on regulatory matters.

5. Independence

5.1 Introduction

The APB Ethical Standards and ISA (UK and Ireland) 260 'Communication of audit matters with those charged with governance', requires us to communicate with you on a timely basis on all significant facts and matters that bear on our independence and objectivity. The Ethical Standards, as revised in December 2010, require that we do this formally both at the planning stage and at the conclusion of the audit, as well as during the audit if appropriate. The aim of these communications is to ensure full and fair disclosure by us to those charged with your governance on matters in which you have an interest.

Required communications	
Planning stage	Final stage
<p>The principal threats, if any, to objectivity and independence identified by EY including consideration of all relationships between you, your affiliates and directors and us;</p> <p>The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality Review;</p> <p>The overall assessment of threats and safeguards;</p> <p>Information about the general policies and process within EY to maintain objectivity and independence.</p>	<p>A written disclosure of relationships (including the provision of non-audit services) that bear on our objectivity and independence, the threats to our independence that these create, any safeguards that we have put in place and why they address such threats, together with any other information necessary to enable our objectivity and independence to be assessed;</p> <p>Details of non-audit services provided and the fees charged in relation thereto;</p> <p>Written confirmation that we are independent;</p> <p>Details of any inconsistencies between APB Ethical Standards, the Audit Commission's Standing Guidance and your policy for the supply of non-audit services by EY and any apparent breach of that policy; and</p> <p>An opportunity to discuss auditor independence issues.</p>

During the course of the audit we must also communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of our safeguards, for example when accepting an engagement to provide non-audit services.

We also provide information on any contingent fee arrangements, the amounts of any future contracted services, and details of any written proposal to provide non-audit services;

We ensure that the total amount of fees that EY and our network firms have charged to you and your affiliates for the provision of services during the reporting period are disclosed, analysed in appropriate categories.

5.2 Relationships, services and related threats and safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including any principal threats. However we have adopted the safeguards below to mitigate these threats along with the reasons why they are considered to be effective.

Self-interest threats

A self-interest threat arises when EY has financial or other interests in your entity. Examples include where we have an investment in your entity; where we receive significant fees in respect of non-audit services; where we need to recover long outstanding fees; or where we enter into a business relationship with the Pension Fund.

At the time of writing, there are no long outstanding fees.

We believe that it is appropriate for us to undertake permissible non-audit services, and we will comply with the policies that the Pension Fund has approved and that are in compliance with the Audit Commission's Standing Guidance.

At the time of writing, there are no non-audit fees. No additional safeguards are required.

A self-interest threat may also arise if members of our audit engagement team have objectives or are rewarded in relation to sales of non-audit services to the Pension Fund. We confirm that no member of our audit engagement team, including those from other service lines, is in this position, in compliance with Ethical Standard 4.

There are no other self-interest threats at the date of this report.

Self-review threats

Self-review threats arise when the results of a non-audit service performed by EY or others within the EY network are reflected in the amounts included or disclosed in the financial statements.

There are no other self-review threats at the date of this report

Management threats

Partners and employees of EY are prohibited from taking decisions on behalf of management of your entity. Management threats may also arise during the provision of a non-audit service where management is required to make judgements or decisions based on that work.

There are no management threats at the date of this report.

Other threats

Other threats, such as advocacy, familiarity or intimidation, may arise.

There are no other threats at the date of this report.

Overall Assessment

Overall we consider that the adopted safeguards appropriately mitigate the principal threats identified, and we therefore confirm that EY is independent and the objectivity and independence of Baldeep Singh, the audit engagement Partner and the audit engagement team have not been compromised.

5.3 Other required communications

EY has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained.

Details of the key policies and processes within EY for maintaining objectivity and independence can be found in our annual Transparency Report, which the firm is required to publish by law. The most recent version of this report is for the year ended 27 June 2014 and can be found here:

<http://www.ey.com/UK/en/About-us/EY-UK-Transparency-Report-2014>

Appendix A Fees

A breakdown of our agreed fee is shown below.

	Planned Fee 2014/15 £	Out-turn 2013/14 £	Published fee 2013/14 £	Explanation
Total Audit Fee – Code work	21,000	22,449	21,000	Extra work due to delays in receipt of, and multiple iterations of, analytics data
Non-audit work	0	0	0	

All fees exclude VAT.

The agreed fee presented above is based on the following assumptions:

Officers meeting the agreed timetable of deliverables;

The operating effectiveness of the internal controls for the key processes outlined in section 4.2 above;

We can rely on the work of internal audit as planned;

Our accounts opinion being unqualified;

Appropriate quality of documentation is provided by the Pension Fund; and

The Pension Fund has an effective control environment.

If any of the above assumptions prove to be unfounded, we will seek a variation to the agreed fee. This will be discussed with the Pension Fund in advance.

Fees for the auditor's consideration of correspondence from the public and formal objections will be charged in addition to the scale fee.

Appendix B UK required communications with those charged with governance

There are certain communications that we must provide to the General Purposes Committee. These are detailed here:

Required communication	Reference
Planning and audit approach Communication of the planned scope and timing of the audit including any limitations.	Audit Plan
Significant findings from the audit Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures Significant difficulties, if any, encountered during the audit Significant matters, if any, arising from the audit that were discussed with management Written representations that we are seeking Expected modifications to the audit report Other matters if any, significant to the oversight of the financial reporting process	Report to those charged with governance
Misstatements Uncorrected misstatements and their effect on our audit opinion The effect of uncorrected misstatements related to prior periods A request that any uncorrected misstatement be corrected In writing, corrected misstatements that are significant	Report to those charged with governance
Fraud Enquiries of the General Purposes Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity Any fraud that we have identified or information we have obtained that indicates that a fraud may exist A discussion of any other matters related to fraud	Report to those charged with governance
Related parties Significant matters arising during the audit in connection with the entity's related parties including, when applicable: Non-disclosure by management Inappropriate authorisation and approval of transactions Disagreement over disclosures Non-compliance with laws and regulations Difficulty in identifying the party that ultimately controls the entity	Report to those charged with governance
External confirmations Management's refusal for us to request confirmations Inability to obtain relevant and reliable audit evidence from other procedures	Report to those charged with governance
Consideration of laws and regulations Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off Enquiry of the General Purposes Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the General Purposes Committee may be aware of	Report to those charged with governance

Required communication	Reference
<p>Independence</p> <p>Communication of all significant facts and matters that bear on EY's objectivity and independence</p> <p>Communication of key elements of the audit engagement director's consideration of independence and objectivity such as:</p> <ul style="list-style-type: none"> The principal threats Safeguards adopted and their effectiveness An overall assessment of threats and safeguards Information about the general policies and process within the firm to maintain objectivity and independence 	<p>Audit Plan</p> <p>Report to those charged with governance</p>
<p>Going concern</p> <p>Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:</p> <ul style="list-style-type: none"> Whether the events or conditions constitute a material uncertainty Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements The adequacy of related disclosures in the financial statements 	<p>Report to those charged with governance</p>
<p>Significant deficiencies in internal controls identified during the audit</p>	<p>Report to those charged with governance</p>
<p>Fee Information</p> <ul style="list-style-type: none"> Breakdown of fee information at the agreement of the initial audit plan Breakdown of fee information at the completion of the audit 	<p>Audit Plan</p> <p>Report to those charged with governance</p> <p>Annual Audit Letter if considered necessary</p>

EY | Assurance | Tax | Transactions | Advisory

Ernst & Young LLP

© Ernst & Young LLP. Published in the UK.
All Rights Reserved.

The UK firm Ernst & Young LLP is a limited liability partnership registered in England and Wales with registered number OC300001 and is a member firm of Ernst & Young Global Limited.

Ernst & Young LLP, 1 More London Place, London, SE1 2AF.

ey.com

This page is intentionally left blank